Property Casualty Insurers
Association of America

Shaping the Future of American Insurance

# NORTH CAROLINA
# LEGISLATIVE RESEARCH COMMISSION SUBCOMMITTEE

## MARCH 21, 2012

## PCI STATEMENT REGARDING
## PROPERTY INSURANCE RATEMAKING
## IN NORTH CAROLINA

The Property Casualty Insurers Association of America (PCI) appreciates the opportunity to submit written testimony before the North Carolina Legislative Research Commission Subcommittee on property insurance ratemaking in the state. PCI is the leading property casualty trade association, representing more than 1,000 insurers, the broadest cross-section of insurers of any national trade association. Our members write more than 38 percent of the property insurance in North Carolina and more than 40 percent of all the property casualty insurance in the state.

North Carolina House Bill (HB) 1305, as passed in 2009, contained a number of provisions that helped to make significant improvements to the North Carolina Beach Plan. Specifically, the provisions of HB 1305 improved the long-term viability of the NC Beach Plan by: 1) slowing the growth in exposure, 2) increasing surplus, 3) strengthening reinsurance requirements, and 4) limiting member liability through the assessment plan. While HB 1305 made great strides toward improving the insurance marketplace, PCI respectfully recommends that the Legislative Study Committee consider additional policy solutions to further strengthen the North Carolina insurance market.

PCI agrees with and strongly supports the conclusions presented by Nancy Watkins, with Milliman, at the meeting today. Specifically, it was noted that rate levels have been suppressed for Homeowners and Dwelling insurance. Artificially suppressed rates discourage insurers from writing new business policies in North Carolina.

The Committee should consider implementation of a flex-rating program. Flex-rating programs permit insurers to increase or decrease rates within a certain percentage without seeking formal approval from the insurance commissioner. Such a program would provide more flexibility to insurers already doing business in North Carolina; likely attract more insurers to the state, increase competition, and lower insurance premiums for many policyholders.

However, PCI believes that such a program is just the beginning. We believe that the flex-rating provision should sunset after a period of 5 years and be replaced by an "open rating" environment in North Carolina. PCI believes that during the flex-rating term, an insurer's dependence and use of the North Carolina Rate Bureau should diminish and when the move to an "open rating" environment is made, use of the NCRB should be optional for all insurers. At that time, the insurers that truly bear the risk of loss should have the freedom (and the experience) to establish their own rates in North Carolina. North Carolina is the **only** state that has a rate bureau for property insurance. An open rating system would maximize competition, and is consistent with the rate making process currently in place everywhere else in the country.

Territorial rating, i.e., classifying risks by geographical location, has long been used in the pricing of insurance rates. Because of wide cost differences occurring in different areas due to events such as hurricanes, earthquakes and wildfires, insurance companies must be able to distinguish regions with greater loss potential from those with less.

In order to achieve price equity among policyholders, companies must be able to rate on the basis of the risk insured. The greater the exposure to an insurable loss, the higher should be the premium. If rates do not reflect costs, subsidies will occur whereby lower-risk policyholders must pay more to offset the losses of higher-risk policyholders. This is precisely what has happened in North Carolina, since rates are the same for all residents of the same county.

Therefore, PCI supports territorial deviations from, with actuarial justification, the North Carolina Rate Bureau established territories. Again, a significant number of policyholders would benefit from such flexibility.

Catastrophe modeling is another tool that has been used, with increasing frequency, to determine maximum probable losses from a single event or multiple events in a single season. This important tool is helpful for insurers, the Plan and the buying public in estimating the exposure to loss from an event.

Catastrophe modeling results when combined with appropriate reinsurance purchases should be accepted and recognized as part of the ratemaking process. These tools provide forward-looking protection for insurers, and in turn, the policyholders. Catastrophe models allow insurers to appropriately reflect the risk assumed and reinsurance allows insurers to write more business while assuring the policyholders and the state that the company will be able to respond to its obligations following a major catastrophic event.

Automatic approval of rate changes reflecting Beach Plan assessments as well as a method, such as post-event bonds, to address losses in excess of available funds for significant catastrophes should also be part of the Committee's recommendations.

**Conclusion**

In order to limit further marketplace disruption, now time to take the next step and move toward a more market-driven approach to property insurance pricing. More must be done with respect to improving rate equity especially in the coastal counties of the state. Unless something is done to permit actuarially sound homeowners rates, there will continue to be forced subsidies for the vast majority of policyholders living along the coast at the expense of those living inland.

PCI would like to thank you for holding these meetings to discuss the topic of property insurance ratemaking, and for allowing Ms. Watkins to testify.

PCI recognizes the complexity of issues involved with the ratemaking process, and appreciates the opportunity to work with the Legislative Study Committee on promoting a viable private insurance market in North Carolina.

Respectfully submitted:

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